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Supreme Court, U.S.
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IN THE

Supreme Court of the United States

ENRON POWER MARKETING, INC.,
Petitioner,

v.

FEDERAL ENERGY REGULATORY COMMISSION, *et al.*,
Respondents.

CORRECTED COPY

STATE OF NEW YORK, *et al.*,
Petitioners,

v.

FEDERAL ENERGY REGULATORY COMMISSION, *et al.*,
Respondents.

BRIEF ON THE MERITS OF RESPONDENTS THE ELECTRICITY CONSUMERS RESOURCE COUNCIL, *ET AL.*

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27 pp

QUESTION PRESENTED

Whether the Federal Energy Regulatory Commission (FERC), which has jurisdiction over interstate transmission of electricity, is obliged to regulate such transmission for sales to retail customers on a bundled basis to remedy undue discrimination and to promote reliability of the interstate grid.

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STATE OF NEW YORK, *et al.*,

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FEDERAL ENERGY REGULATORY COMMISSION, *et al.*,

Respondents.

BRIEF ON THE MERITS OF RESPONDENT INDUSTRIAL CONSUMERS (THE ELECTRICITY CONSUMERS RESOURCE COUNCIL, AMERICAN IRON AND STEEL INSTITUTE, AND AMERICAN CHEMISTRY COUNCIL)

OPINION BELOW

The opinion of the United States Court of Appeals for the District of Columbia Circuit is reported at 225 F.3d 667 (D.C. Cir. 2000), and reprinted at Petitioner's Appendix (Pet. App.) 3a to 121a. Federal Energy Regulatory Commission Order No. 888 is reported at F.E.R.C. Stats. & Regs. ¶ 31,036, 61 Fed. Reg. 21, 540 (1996). FERC's rehearing decisions, Order No. 888-A and Order No. 888-B, are reported respectively at III F.E.R.C. Stats. & Regs. ¶ 31,048, 62 Fed. Reg. 12,274 (1997), and 81 F.E.R.C. ¶ 61,248, 62 Fed. Reg. 64,688 (1997). Relevant portions of FERC Orders Nos. 888 and 888-A and FERC's Notice of Proposed Rulemaking, F.E.R.C. Stats. & Regs. ¶ 32,514, 60 Fed. Reg. 17,662 (1995), are reprinted at Pet. App. 125a to 654a.

JURISDICTION

The court of appeals entered its judgment on June 30, 2000, and issued its order denying a timely-filed motion for rehearing on August 22, 2000. This Court has jurisdiction under 28 U.S.C. § 1254(l).

STATUTES AND REGULATIONS INVOLVED

Sections 201, 205, 206, 211, 212, 213, and 313 of the Federal Power Act (FPA), 16 U.S.C. §§ 824, 824d, 824e, 824j, 824k, 824l and 825l, are reprinted in the Appendix at Pet. App. 652a to 681a.

Sections 1, 4, and 5 of the Natural Gas Act (NGA), 15 U.S.C. §§ 717, 717c, and 717d, are reprinted in the Appendix at Pet. App. 645a to 651a.

Relevant portions of FERC Orders Nos. 888 and 888-A are reprinted in the Appendix at Pet. App. 125a to 551a.

STATEMENT

FERC has found that vertically-integrated electric utilities have an incentive to deny use of the transmission wires that are an essential facility to deliver power to markets by providing transmission service to their own customers to the detriment of competing suppliers. In FERC Order No. 888, FERC found that transmission-owning utilities have an inherent incentive to discriminate, and have discriminated, against competing suppliers that are dependent on the utilities for transmission services. Pet. App. 213a-216a, 315a-331a. Based on this finding, FERC required utilities to file an "open access transmission tariff" (OATT) and to take transmission services for their own wholesale sales under the OATT pursuant to the same terms and conditions they offer to other users. Pet. App. 178a.[1] But FERC declined to apply this requirement to a utility's transmission services when the charge for power transmitted and distributed to retail customers is a single "bundled" charge that includes both the price of power and transmission. By declining to apply the OATT to transmission for bundled retail sales, FERC has failed to deal with the majority of transmissions that are the source of undue discrimination that FERC itself has found. Almost 60 percent of retail sales by investor-owned utilities and

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[1] FERC applied this same requirement to unbundled retail sales, i.e., retail transactions in which the utility, either voluntarily or under compulsion at requirement of state law, states separate charges for the electric energy and for the service of transmitting the energy. Pet. App. 306a.

independent power producers are bundled.[2] Thus, FERC left the IOUs free to ignore the OATT, and discriminate in favor of their own retail customers, with respect to a very high percentage of the use of their transmission facilities.

FERC claimed in Order No. 888-A that it lacks jurisdiction to address discrimination in transmission associated with bundled retail sales. *See* Pet. App. 454a-456a. The court of appeals upheld FERC's discretion to determine that it lacked jurisdiction over interstate transmission for bundled retail sales.

A. Interest Of Industrial Consumers

The Electricity Consumers Resource Council (ELCON) is an association of industrial consumers of electricity organized to promote the development of

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[2] In 1999, approximately 2.44 billion megawatt hours of electricity were sold at retail by FERC jurisdictional generators: 2.4 billion by investor-owned utilities (IOUs) plus 43 million by independent power producers (IPPs). *See* Energy Information Administration, United States Department of Energy (EIA), Financial Statistics of Major U.S. Publicly Owned Electric Utilities 1999, at 3 (2000); EIA, Electric Power Annual 1999, Vol. 2, at 87 (2000). At most, 915 million of these megawatt hours, or 37.5%, had previously been sold at wholesale. *Id.* (showing 545 million megawatt hours were available for resale by IOUs and 370 million megawatt hours were sold "to Utilities" by IPPs). About 76 million megawatt hours (3% of retail sales) were sold on an unbundled basis, with the remaining 97% sold on a bundled basis. *See* EIA, Electric Sales and Revenue 1999 at 3 (2000) (noting that total retail sales were generally made on a bundled basis); Electric Sales and Revenue 1999, at 245, 255 (2000) (showing transmissions of 76 million megawatt hours sold pursuant to "retail wheeling" programs, i.e., on an unbundled basis). In total, therefore, almost 60% (1.45 billion of 2.44 billion megawatt hours) of pertinent transmissions were bundled with retail sales.

coordinated and rational federal and state policies that will assure an adequate, reliable and efficient electricity supply for all users at competitive rates and prices. ELCON member companies produce a wide range of products, including: steel, aluminum, chemicals, petroleum, motor vehicles, industrial gases, machinery, glass, agricultural and food products, rubber, computer chips, paper and electronics. The member companies of ELCON consume approximately 5 percent of all electricity in the United States.

The American Iron and Steel Institute (AISI) is the principal trade association of the North American steel industry. Its member companies account for about 70 percent of the raw steel production in the United States. The steel industry is one of the most energy-intensive sectors in the United States; the cost of electricity for AISI members may constitute as much as 20 percent of the manufacturing cost of a steel mill product.

The American Chemistry Council (ACC) is a nonprofit trade association whose member companies represent more than ninety percent of the productive capacity of basic industrial chemicals in the United States. The manufacturing processes of many ACC member companies are highly energy-intensive. In addition, the chemical industry uses a substantial amount of self-generated electricity. Total electricity used by the industry, purchased plus self-generated, represents approximately 18 percent of industrial electricity consumption in the United States and approximately 6 percent of national electricity consumption.

Industrial Consumers are vitally concerned to have access to power supplies that are both reliable and low-cost. Recent events in California and other sections of the

country show the absolute urgency of maximizing the efficiency and reliability of the interstate grid. With respect to reliability, interruption in power supplies can have significant economic consequences. In the case of some industries, even momentary interruptions can yield losses of hundreds of thousands of dollars.

The cost of power represents an equally important consideration. Industrial Consumers must be able to enjoy the benefit of competition among available suppliers in electricity as with respect to other commodities and raw materials in order to be able to compete in international markets. It is essential to Industrial Consumers' own ability to compete that FERC eliminate discriminatory access to transmission facilities. Ending such discrimination is an essential condition to the development of competitive markets. Industrial Consumers, Enron, and other parties have long advocated that FERC conduct a rulemaking to assure that transmission providers are required to provide service to retail "native load" customers under the Order No. 888 OATT.[3] Discrimination will persist in the electric power industry until all transmission service, wholesale and retail, is subject to the same tariff. FERC's parsimonious view of its statutory mandate has prevented it from acting to assure

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[3] On March 25, 1998, Enron, ELCON, and a coalition of power marketers and independent power producers filed a petition with FERC for a rulemaking that would require that all uses of the transmission service be subject to the OATT. The coalition asked FERC to unbundle transmission operationally from all merchant functions, including sales to captive native-loaded customers. *See* Petition for a Rulemaking on Electric Power Industry Structure and Commercial Practices and Motion to Clarify or Reconsider Certain Open-Access Commercial Practices, FERC Docket No. RM98-5-000 (1998). FERC never acted on the petition.

that all uses of the transmission grid are subject to the same set of rules.

B. Statutory Background

The FPA gives FERC jurisdiction over "the transmission of electric energy in interstate commerce" and "all facilities for such transmission." FPA § 201(b), 16 U.S.C. § 824(b). It also gives FERC jurisdiction over "the sale of electric energy at wholesale in interstate commerce." *Id.* Unlike its jurisdiction over the sale of electricity, FERC's jurisdiction over interstate "transmission" is not limited by the words "at wholesale." *See* Pet. App. 338a.

Section 205(b) of the FPA, 16 U.S.C. § 824d(b), bars any public utility, "with respect to any transmission or sale subject to the jurisdiction of the Commission," from "grant[ing] any undue preference or advantage to any person or subject[ing] any person to any undue prejudice or disadvantage" and requires each utility to file tariffs setting forth its "practices." Section 206(a), 16 U.S.C. § 824e(a), commands that if FERC determines that a practice is "unjust, unreasonable, unduly discriminatory or preferential," FERC must cure the discrimination and "determine the just and reasonable . . . practice . . . to be thereafter observed and in force, and shall fix the same by order."

C. Proceedings Below

In *Transmission Access Policy Study Group v. FERC*, 225 F.3d 667, 681, 687 (D.C. Cir. 2000), Pet. App. 8a-9a, 20a-21a, the court of appeals considered, on the one hand, the claim by state groups that FERC had exceeded its jurisdictional reach in Order No. 888 and, on the other hand,

the claim by Petitioner Enron that FERC interpreted its jurisdiction too narrowly. The State of New York and other parties contended that FERC has no jurisdiction over interstate transmission for any retail sales, even unbundled sales. The D.C. Circuit rejected this contention, holding that the Act confers jurisdiction over unbundled interstate transmission of electric energy whether it is then sold at wholesale or retail. Pet. App. 34a-35a.

With respect to Petitioner Enron's opposite argument that FERC has jurisdiction over bundled retail sales, the court acknowledged that it was a plausible reading of the FPA to construe transmission "bundled with generation and delivery services and sold to a consumer for a single charge as . . . transmission services in interstate commerce" within FERC's jurisdiction. Pet. App. 35a. [4] However, the court ruled that FERC's decision to decline jurisdiction over interstate transmission of electric energy for bundled retail sales was a "permissible policy choice" as to which FERC was entitled deference under *Chevron, U.S.A., Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837, 842-43 (1984). Pet. App. 35a.

ARGUMENT

Section 201(b) of the FPA grants FERC jurisdiction over "the transmission of electric energy in interstate commerce and ... all facilities for such transmission." 16 U.S.C. § 824(b), Pet. App. 652a.[5] The

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[4] Industrial Consumers endorse the legal argument presented by Petitioner Enron Power Marketing, Inc., in its Petition for Certiorari.

[5] The transmission of "electric energy in interstate commerce" is defined in the FPA as electric energy "transmitted in interstate commerce if transmitted from a State and consumed at any point outside thereof; but

statute contains no limitation on the Commission's jurisdiction over interstate transmission: only "local distribution" is reserved to the states. *See id.* FERC's jurisdiction over interstate transmission is not limited to wholesale transactions. *See FPC v. Louisiana Power & Light Co.*, 406 U.S. 621, 636 (1972) (interpreting analogous provisions of the Natural Gas Act ("NGA"), 15 U.S.C. §§ 717, *et seq.*).

FERC's exercise of its authority over all interstate transmission is needed to assure a single set of rules for the road to govern interstate transmission—the highways by which electric power is distributed to market. The reliability of the transmission grid will be jeopardized if there is balkanization of regulatory control over bundled retail transmission between FERC and each individual state. FERC jurisdiction over all interstate transmission is also essential to avoid discrimination by transmission-owning utilities. Unless discrimination is eliminated with respect to the great majority of transmission associated with bundled retail sales, competitive power markets cannot develop.

I. To Assure A Reliable Interstate Transmission Grid, FERC Must Exercise Authority Over Bundled Retail Transmission

FERC exercise of its jurisdiction over bundled retail transmission is necessary to ensure the growth of competition in interstate power markets, and to prevent balkanization of the transmission grid. Federal jurisdiction over bundled retail transmission need not intrude on

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only insofar as such transmission takes place within the United States." 16 U.S.C. § 824(c), Pet. App. 653a.

appropriate areas of state regulation such as retail price regulation, certificating generation or local siting authority or the decision whether to adopt restructuring laws which may require utilities to divest generation or to institute retail customer choice. However, FERC exercise of its jurisdiction over transmission will allow consistency in determination of available transmission capacity, in congestion management, and in ascertaining the conditions under which transmission will be interrupted or curtailed.

A regime under which each state can set its own rules for operating the transmission system used to make bundled retail sales within that state is counterproductive to rational and coherent transmission regulation. The absence of a single regulator enables one state to favor transmission to its own residents, at the expense of its neighbors and at the expense of power destined for wholesale or unbundled retail transactions. The pernicious impact of allowing parochial and inconsistent administration of the interstate grid is intuitive and easily illustrated. In a time of congestion on an interstate highway, surely it would be intolerable for the state troopers of a given state to favor their own residents and require motorists with out-of-state license plates to exit the highway.[6] If anything, the consequences of chauvinistic state action are even more dire in electricity, as power does not flow simply from point to point but follows the path of least resistance. There are no side roads; power cannot be stored; and power inevitably

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[6] *The Electricity Competition and Reliability Act: Hearing on H.R. 2944 Before the House Subcommittee on Energy and Power of the House Committee on Commerce*, 106th Cong. 77-79 (1999) (statement of FERC Commissioner William Massey).

moves through interstate transmission wires in an interconnected interstate grid.

The existing patchwork of inconsistent and outdated jurisdictional rules for this essential interstate delivery system, coupled with splintered network management, create obstacles and uncertainties that prevent development of a competitive market for electric power. If buyers and sellers lack confidence that electric power will be delivered reliably and on reasonable terms and conditions, they will not transact business.[7]

FERC Commissioner William Massey explained in testimony before the Senate Committee on Energy and Natural Resources:

> Electric power markets are inherently interstate in nature. The laws of physics, and hence power markets, do not respect state boundaries. In order to thrive, such markets must have an open, non-discriminatory, well-managed, and efficiently priced interstate transmission service that links buyers and sellers of power.

Electricity Deregulation: Hearing Before the Senate Committee on Energy and Natural Resources, 106th Cong. 183-88 (2000). Former FERC Chairman James Hoecker has similarly expressed concern that "divide[d] authority over reliability measures among states and between the states,

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[7] Br. for the State Public Service Commissions In Opp'n, Jan. 26, 2001.

FERC and the industry threatens efficiency and indeed even reliability itself."[8]

FERC's failure to exercise its jurisdiction over bundled retail transmission threatens the orderly administration of the transmission grid and jeopardizes reliability of transmission service for all consumers.

II. Unless FERC Exercises Jurisdiction Over All Interstate Transmission, Including Bundled Retail Transmission, Discrimination Will Persist

A. FERC Has A Duty To Address Anticompetitive Practices That Fall Within Its Jurisdiction

In Order No. 888, FERC acknowledged that the FPA, like the NGA, "'fairly bristles' with concern for undue discrimination." Pet. App. 181a-182a, citing *Associated Gas Distribs. v. FERC*, 824 F.2d 981, 998 (D.C. Cir. 1987). *See also Gulf States Util. Co. v. FPC*, 411 U.S. 747, 758-59 (1973), *reh'g denied* 412 U.S. 944 (1973); *Alabama Power Co. v. FPC*, 511 F.2d 383 (D.C. Cir. 1974).

In *FPC v. Conway Corp.*, 426 U.S. 271 (1976), this Court considered whether the Federal Power Commission's (FPC's) authority, and responsibility, under §§ 205 and 206 of the FPA, extends to claims of discrimination between rates for two classes of service, only one of which is subject to the jurisdiction of the

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[8] "Reassessing Regulation in Light of Markets," Remarks of (former) Chairman James Hoecker, Mid-America Regulatory Commissioners Annual Meeting, June 12, 2000, at http://www.ferc.fed.us.

Commission. The FPC had determined that it could not address price squeeze claims. This Court rejected the FPC's position as "untenable." *Id.* at 277. The FPC has "jurisdiction to consider the allegations of the company's wholesale customers that the proposed wholesale rates, which are within the Commission's jurisdiction, are discriminatory and noncompetitive when considered in relation to the company's retail rates, which are not within the jurisdiction of the Commission." *Id.* at 272-73. The Court observed:

> The Commission thus cannot so easily satisfy its obligation to eliminate unreasonable discriminations or put aside its duty to consider whether a proposed rate will have anticompetitive effects. *The exercise by the Commission of powers otherwise within its jurisdiction "clearly carries with it the responsibility to consider, in appropriate circumstances, the anticompetitive effects of regulated aspects of interstate utility operations pursuant to . . . directives contained in §§ 205, 206. . . ."* *Gulf States Util. Co. v. FPC*, 411 U.S. 747, 758-759 (1973).

Id. at 278-279 (emphasis added).

In the case of electricity, as in natural gas, FERC has a statutory mandate to eliminate anticompetitive practices in interstate transmission.

B. FERC Cannot Address Discrimination In Transmission Without Exercising Jurisdiction Over Transmission Associated With Bundled Retail Sales

1. In The Order No. 888 Rulemaking, FERC Recognized The Potential For Discrimination Resulting From Excluding Bundled Retail Transmission From the OATT

FERC recognized in Order No. 888 that vertically-integrated utilities are motivated to discriminate in providing transmission access to their competitors:

> It is in the economic self-interest of transmission monopolists, particularly those with high-cost generation assets, to deny transmission or to offer transmission on a basis that is inferior to that which they provide themselves. The inherent characteristics of monopolists make it inevitable that they will act in their own self-interest to the detriment of others by refusing transmission and/or providing inferior transmission to competitors in the bulk power markets to favor their own generation, and it is our duty to eradicate unduly discriminatory practices.

Pet. App. 213a-214a.

In the notice of proposed rulemaking, the Commission recognized that if bundled retail service were not made subject to the OATT, then utilities will provide service

> . . . under two separate arrangements – an explicit wholesale transmission tariff filed at the Commission and an implicit retail transmission tariff governed by a state regulatory body. It also raises the possibility that the quality of transmission service for retail purposes will be superior to the quality of transmission service offered for wholesale purposes.

Promoting Wholesale Competition through Open Access Non-Discriminatory Transmission Services by Public Utilities, Notice of Proposed Rulemaking, IV F.E.R.C. ¶ 32,514 at 33,081-82 (1995), Pet. App. 634a. FERC found that "unduly discriminatory and anticompetitive practices exist today in the electric industry." Order No. 888, Pet. App. 213a. *See also* Order No. 888-A, Pet. App. 382a. "[T]he vast majority of utilities historically have declined to transport electric energy that would compete with their own sales or have offered access that is inferior to what they use for their own sales." Order No. 888-A, Pet. App. 436a-437a. Structural conditions in the industry "make it inevitable" that transmission owners will "act in their own self-interest to the detriment of others by refusing transmission and/or providing inferior transmission to competitors." Order No. 888, Pet. App. 213a-214a.

Because FERC has jurisdiction over all interstate transmission, and because FERC has found that utilities have the motive and the opportunity to discriminate in transmission services, the court of appeals erred in deferring to FERC's determination not to exercise its jurisdiction to remedy the discrimination that it found with respect to the majority of transmission uses: those bundled with retail sales.

2. The Same Authority That The Commission Exercised Under The NGA To Extend Nondiscriminatory Open Access to Natural Gas Retail Customers Is Available Under the FPA

Following introduction of open-access pipeline transportation in Order No. 436, discrimination persisted and lack of service comparability plagued gas markets:

> [T]he firm transportation embedded within the *pipelines' bundled, city-gate, firm sales service is superior* to the pipeline's open-access firm transportation service. This means that pipelines and other gas suppliers are not competing on an even basis for sales customers, even where firm transportation is available to move the gas sold by the pipelines' competitors.

Pipeline Service Obligations and Revisions to Regulations Governing Self-Implementing Transportation; and Regulation of Natural Gas Pipelines after Wellhead Decontrol, Order No. 636, [1991-96 Regs. Preambles] F.E.R.C. Stats. & Regs. ¶ 30,939 at 30,402 (emphasis added). Not until FERC issued Order No. 636 and unbundled transportation completely from both the pipeline's wholesales and its direct retail sales was it able to achieve "an even basis for competition." *Id.*

Open access alone did not eliminate the incentives for pipelines to discriminate in favor of their own sales and against third-party shippers. Similarly, wholesale open-access electricity transmission does not establish comparability between the bundled transmission service that transmission-owning utilities use to serve their captive customers and the wholesale and unbundled retail transmission services that they provide to others. As Mr. Hoecker noted: "Recognizing the states' keen interest in ensuring that native load is not disadvantaged in the wholesale competition environment," FERC will "only be able to promote real competition to the extent that *all* uses of the grid and *all* transmission facilities are subject to the same non-discriminatory rules."[9]

With respect to the natural gas industry, FERC determined that in order to eliminate the incentive of a regulated transportation monopolist to discriminate in favor of its own and affiliated generation, it was necessary to make the merchant operation take transportation pursuant to rules identical to the rules that govern all other shippers. FERC's erroneous view of the parameters of its jurisdiction under the FPA is preventing the Commission from taking necessary

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[9] Remarks of James Hoecker, *supra* (emphasis in original).

steps to eliminate discrimination in the electric power industry.

In July 2000, FERC commissioned a staff report on the state of regional bulk power markets due to FERC's grave concern with poorly-functioning markets. FERC observed that it was incumbent on the Commission to take steps to investigate malfunctioning markets and serious price volatility. *See* Order Directing Staff Investigation, 92 FERC ¶ 61,160 (July 26, 2000).

On November 1, 2000, FERC issued its report, "Investigation of Bulk Power Markets – Midwest Region." FERC's Staff Report on the Midwest markets recommends that FERC:

> [r]educe the advantages of network service over point-to-point service by requiring that native load be served under the same tariff provisions as other transmission services. Given that all transactions serve load of one sort or another, all load would be treated in the same manner. This would eliminate the current incentives that vertically integrated transmission owners have to favor their native load through the manner and method of calculating ATC [available transmission capacity] and handling interconnection requests. It would also restore confidence among market participants that transmission owners were not calling TLRs [a form of

> service curtailment] to favor native load, because they would no longer have the incentive to do so.[10]

The Staff Report goes on to find:

> [M]any vertically integrated transmission owners may have incentives to resist efforts to make this information [on available transmission capacity] transparent and standardized, including information on the manner in which "native load" is handled in making these calculations. . . . As a consequence, the Commission may wish to eliminate the native load exemption and have all transactions under the same tariff. Given that all transactions serve load of one sort or another, all load would be treated in the same manner. This would provide all transmission owners the proper incentives to make relevant information available.[11]

In Order No. 888-A, FERC stated that "[t]he record supports our conclusion that absent open access, undue discrimination will continue to be a fact of life in today's and tomorrow's electric power markets." Pet. App. 382a. The record at the time of the Order No. 888 rule and

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[10] FERC, Staff Investigation of Bulk Power Markets: Midwest Region at 49 (Nov. 2000).

[11] *Id.* at 40.

the Agency's own reports since that date demonstrate that vertically integrated transmission-distribution utilities have a strong incentive to restrict the access of both wholesale and potential retail competitors to the transmission capacity that they control. Discrimination is ongoing and will persist until there is complete unbundling and consumers of all transmission services, wholesale and retail, take service pursuant to the same tariff at posted rates. FERC's unduly restrictive reading of its own jurisdiction prevents it from acting to remedy this discrimination.

CONCLUSION

The court of appeals' decision should be reversed.

Respectfully submitted,

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